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FEDERAL COMMUNICATIONS COMMISSION
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Before The
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Accounting for Judgments and Other Costs Associated with Litigation	)	CC Docket No. 93-240
	)	
	)	

COMMENTS OF BELLSOUTH

BELLSOUTH TELECOMMUNICATIONS, INC.

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List A B C D E

TABLE OF CONTENTS

SUMMARY

BellSouth strongly opposes the accounting and ratemaking rules proposed in the Notice. The "ratepayer benefit" standard articulated in the Notice is contrary to more than a half-century of jurisprudence, which establishes that operating expenses that are ordinary and necessary to operate a public utility must be permitted to be recovered in rates unless "imprudently" or "inefficiently" incurred. In effect, the proposed rules create a presumption that any action by carrier management that is ultimately adjudged to have violated a federal statute was *per se* imprudent. Such a presumption is clearly contrary to the established jurisprudence.

The proposed rules are unnecessary. The proposed accounting rules are in direct conflict with GAAP, and with the accounting principles articulated by the Commission in Part 32. The deferred accounting proposed for other antitrust litigation costs will increase carriers' capital requirements and the cost of capital. The Notice neither recognizes these effects nor proposes to compensate investors for these effects. The Commission's proposed accounting rules therefore are arbitrary and capricious. The proposed rules will also create a disparity between SEC and FCC financial reports.

The proposed rules are also contrary to sound ratemaking principles. They will result in under

recognition of costs in some periods and over recognition of costs in other periods. When applied to price cap LECs, the proposed rules could trigger sharing or increase sharing during periods when operating expenses are deferred, and reduce or eliminate sharing in periods when deferred expenses are finally recognized. Whether the proposed rules would result in actual benefit to ratepayers is determined by pure happenstance, since it would depend on the earnings of carriers years after the conduct giving rise to the presumptive disallowance occurred. With regard to price cap LECs, the proposed rule would also double count the disallowance, since the vacated rules were applied during 1990, the year used to establish the initial LEC price cap rates.

The proposed rules are also discriminatory. As proposed in the Notice, the accounting and ratemaking rules would apply only to those carriers subject to Part 32 of the Commission's Rules. However, the Commission also has regulatory jurisdiction over nondominant interexchange carriers, competitive access providers, cable companies and other competitors of the Part 32 carriers. Application of these onerous rules to only one class of carriers, while exempting their competitors from the rules, would be arbitrary and capricious.

The proposed rules will also impose costs on the carriers and their customers that far exceed any possible benefit. BellSouth describes herein the administrative burden that the proposed rule will impose on the carriers, the Commission and the courts. These administrative costs will be incurred whether or not any disallowances occur. BellSouth also describes its experience during the applicability of the vacated rules. During the four years that the vacated rules were applied, BellSouth incurred no adverse antitrust judgments or settlements, and paid only one adverse judgment in a federal labor statute case. Thus, in BellSouth's experience, the proposed rule is unnecessary to protect ratepayers, and the cost of administering the rules will outweigh any perceived benefit.

There are also substantial indirect costs associated with the proposed rules. In addition to the increased capital costs mentioned above, the proposed rule will provide carrier competitors with an advantage unrelated to their business acumen. To the extent that the proposed rules dull the Part 32 carriers' incentives to compete aggressively, ratepayers will suffer.

The Commission should recognize that carrier management is not going to engage in a willful violation of the antitrust laws. However, there is no bright line between aggressive competition and anticompetitive conduct. BellSouth provides a specific, historical example of carrier conduct that was undertaken in good faith and in reliance on ground rules established by the Commission. Two antitrust suits followed. In one, the carriers were found to have violated the antitrust laws. In the other, the carriers' conduct was exonerated. This example highlights that antitrust courts evaluate carrier conduct with 20-20 hindsight, filtered by the rules of evidence and the adversarial process. It is precisely because of such uncertainty that the jurisprudence does not impute a presumption of imprudent management based solely on the outcome of litigation.

The Commission should allow carriers to recover settlement costs, whether the settlement occurs pre- or post-judgment. The law favors settlements. The Commission should not adopt rules that provide incentives for carriers to reject settlements that are otherwise justified because of adverse ratemaking treatment. If settlements are disallowed, the Commission should at least permit the recovery of avoided litigation costs.

The Commission should not require deferred accounting for other antitrust litigation costs. Such costs are ordinary and necessary operating expenses that are prudently incurred and must be recognized in ratemaking. The proposed accounting does not hold these costs outside of ratemaking, as asserted in the Notice, but effectively disallows them for the duration of the litigation, thereby requiring investors to finance the litigation. If the Commission persists in adopting its deferred accounting proposal, it must make provision to compensate investors for the use of their funds during the pendency of the litigation. Furthermore, the Commission should not require deferral accounting until a lawsuit is finally resolved if the count that triggered the application of the rule is dismissed at a preliminary stage of the proceeding.

Even if the Commission adopts its proposed rules for antitrust cases, it should not extend the rules to other statutory violations. In many cases, decisions which are "right" when made, i.e., that are the decisions that ratepayers would have made themselves in their own economic interest, turn out to be "wrong" when finally adjudicated. This does not render the decision imprudent, and does not support a disallowance.

Finally, the interim accounting rule adopted in the Notice is patently unlawful and must be rescinded. Section 220(g) of the Communications Act requires six months advance notice of changes in accounting requirements. Furthermore, the interim action violates the prohibitions against retroactive rulemaking and retroactive ratemaking.

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COMMENTS OF BELLSOUTH

BellSouth Telecommunications, Inc. ("BellSouth") hereby offers it comments on the Notice of Proposed Rulemaking and Order ("Notice"), FCC 93-424, released September 9, 1993.

I. Background.

In 1982, the Commission considered the policy to be followed in connection with the accounting and ratemaking treatment for litigation expenses of common carriers.[1] In its Policy Decision, the Commission acknowledged the judicial requirements for lawful agency ratemaking actions regarding operating expenses:

> [W]e are mindful of judicial ratemaking standards, among them that regulatory commissions should 'give heed to all legitimate expenses that will be charges upon income during the term of the regulation.' West Ohio Gas Co. v. Public Utilities Commission of Ohio, 294 U.S. 63, 74 (1934). While the Commission regulates rates, it does not manage a carrier's business. Good faith is presumed on the part of a carrier's management, and it has been stated that public utility commissions should not substitute their judgments as to the reasonableness of expenses in the absence of a showing of inefficiency or improvidence. See Southwestern Bell Telephone Co.

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[1]In the Matter of Policy to be Followed in the Allowance of Litigation Expenses of Common Carriers in Ratemaking Proceedings, CC Docket No. 79-18; In the Matter of Revisions to the Uniform System of Accounts, CC Docket No. 78-196, Memorandum Opinion and Order, 91 F.C.C. 2d 140 (1982) ("Policy Decision").

v. Public Service Commission of Missouri, 262 U.S. 276, 288-28 (1922); West Ohio Gas Co. v. Public Utilities Commission of Ohio, supra., Monroe Gaslight and Fuel Co. v. Michigan Public Utilities Commission, 11 F.2d 319, 325 (E.D. Mich. 1926). Generally, in determining rate of return, public service commissions must consider the sum required by the utility to meet its operating expenses. They may disallow expenses actually incurred in the company's operation where the challenged expense is found to be exorbitant, unnecessary, wasteful, extravagant, or incurred in the abuse of discretion or in bad faith, or of a nonrecurring nature. Alabama Public Service Commission v. Southern Bell Telephone and Telegraph Co., 42 So.2d 655 (1949). See also AT&T (Docket No. 19129), 64 FCC 2d 1, 85-86 (1977) and Communications Satellite Corporation (Docket No. 16070), 56 FCC 2d 1101, 1174-75 (1975). Pursuant to the provisions of the Communications Act of 1934, as amended, a carrier has the burden of establishing the reasonableness of its operating expenses and must support inclusion of any challenged expenditure. See 47 U.S.C. Sec. 204(a) and 220(c). Thus, under existing ratemaking treatment a carrier can charge ordinary operating expenses incurred in the provision of utility service to the consumer, but must justify as reasonable any questioned expenditure.[2]

After considering whether any new or different accounting or ratemaking treatment of litigation costs was required in the public interest, the Commission terminated the proceeding, concluding:

> We believe that the current ratemaking treatment is adequate protection against unreasonable litigation spending.[3]

Shortly after the Policy Decision was issued, a $276 million adverse judgment was entered against AT&T in an

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[2]Policy Decision, 91 F.C.C. 2d 144-145.

[3]Policy Decision, 91 F.C.C. 2d at 147.

antitrust lawsuit brought by Litton Systems, Inc.[4] At approximately the same time, settlement was reached in the government's antitrust lawsuit against AT&T.[5] The large verdict in Litton and the sizable litigation expenses incurred in both the Litton and government cases apparently caused the Commission to reconsider whether additional accounting and ratemaking rules for antitrust lawsuits were required. The Commission ordered AT&T and the Bell operating companies to account for the judgment and expenses associated with the Litton case in below-the-line accounts.[6] In a rulemaking proceeding the Commission codified below-the-line accounting treatment for antitrust judgments and related costs.[7] The affected carriers appealed both orders. On the same day, the D.C. Circuit Court of Appeals entered

[4]See Litton Sys. v. AT&T, 700 F.2d 785 (2d Cir. 1983), cert. denied, 464 U.S. 1073 (1984).

[5]United States v. AT&T, 552 F.Supp. 131 (D.D.C. 1982), aff'd. sub nom. Maryland v. United States, 460 U.S. 1001 (1983).

[6]AT&T, Ameritech, Bell Atlantic, BellSouth, NYNEX, Pacific Telesis, Southwestern Bell, and U S West--Accounting Instructions for the Judgment and Other Costs Associated with the Litton Systems Antitrust Lawsuit, 98 FCC 2d 982 (1984), recon., 3 FCC Rcd 500 (1988).

[7]In the Matter of Notice of Proposed Rulemaking to Amend Part 31 Uniform System of Accounts for Class A and Class B Telephone Carriers to Account for Judgments and Other Costs Associated with Antitrust Lawsuits, and Conforming Amendments to Annual Report Form M, CC Docket No. 85-64, Notice of Proposed Rulemaking, FCC 85-120, released May 3, 1985, Report and Order, 3 FCC Rcd 3241 (1987), Recon., 4 FCC Rcd 4092 (1989).

decisions in both the Litton Accounting Appeal[8] and the Litton Costs Decision[9], reversing the Commission in both cases.

In the Litton Accounting Appeal, the Court cited the "more than a half-century" of Supreme Court jurisprudence admonishing regulatory agencies to "give heed to all legitimate expenses that will be charges upon income during the term of regulation."[10] The Court also cited its own jurisprudence, noting that "[i]f [expenses are] properly incurred, they must be allowed as part of the composition of the rates. Otherwise, the so-called allowance of a return upon the investment, being an amount over and above expenses, would be a farce."[11] The Court noted that the Commission's own Policy Decision, quoted extensively above, recognized these legal requirements. Finding the requirement for below-the line accounting "a radical departure from its past practice" and the Commission's explanations for the change "intolerably mute", the Court vacated the challenged orders and remanded the case to the

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[8]Mountain States Telephone and Telegraph Company, et al., v. FCC, 939 F.2d 1021 (D.C. Cir. 1991) ("Litton Accounting Appeal").

[9]Mountain States Telephone and Telegraph Co., et al., v. FCC, 939 F.2d 1035 (D.C. Cir. 1991) ("Litigation Costs Decision").

[10]Litton Accounting Appeal, 939 F.2d at 1029.

[11]Id.

Commission.[12] On September 27, 1993, the Commission terminated the proceeding without further action.[13]

In the companion Litigation Costs Decision, the Court vacated the orders adopted in the rulemaking proceeding. The Court held that the Commission's Orders

> must be reversed for two related reasons. First, although the agency set out to change accounting classifications and presumptions with respect to all violations of federal statute law, it did not adequately justify its application of the rules beyond the antitrust context. Second, while the FCC considered in some detail the effect of the rules on the various incentives facing the carriers, there are significant gaps in its analysis. Consequently, the agency's reasoning is not sufficient to support its rule.[14]

In the present proceeding, the Commission proposes to adopt, with some modifications, the treatment of litigation costs previously advanced in the vacated orders. For the reasons set forth below, BellSouth strongly opposes the adoption of rules that would change the way litigation costs are accounted for and treated in ratemaking.

II. The Notice fails to recognize the controlling legal standard for the inclusion of operating expenses in ratemaking.

In the Notice, the Commission repeatedly states a standard for the recovery of operating expenses by a

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[12] Id., 939 F.2d at 1035.

[13] In the Matter of American Tel. and Tel. Co., et al.- Accounting Instructions for the Judgment and Other Costs Associated with the Litton Systems Antitrust Lawsuit, Order on Remand, FCC No. 93-431, released September 27, 1993.

[14] Litigation Costs Decision, 939 F.2d at 1042.

regulated utility that is at marked variance with the controlling legal standard. For example, the Notice states:

> Litigation cost rules are still needed to prevent these LECs from recovering through regulated rates expenses incurred as a result of unlawful conduct that does not benefit ratepayers.[15]

This "ratepayer benefit" standard permeates the Notice. In proposing to require that antitrust settlements be recorded in a nonoperating expense account, the Notice states:

> We also continue to believe that this approach is most consistent with the underlying principle that expenses not incurred for the benefit of ratepayers should not be routinely passed on to ratepayers.[16]

As noted in the quote from the Commission's Policy Decision, above, under longstanding judicial precedent, carriers are entitled to "charge ordinary operating expenses incurred in the provision of utility service to the consumer, but must justify as reasonable any questioned expenditure."[17] The fact that the expenses were incurred in support of regulated operations qualifies them as being appropriate for recovery in regulated rates, absent a showing of "inefficiency or improvidence."[18]

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[15] Notice at para. 7.

[16] Notice at para. 11. See also Notice at paras. 15, 21, 22, 23, 24, 25, and footnotes 37 and 41.

[17] Policy Decision, 91 FCC 2d at 145.

[18] Id. See also Litton Accounting Appeal, 939 F.2d at 1034.

As both panels of the Court of Appeals recognized, the fact that a lawsuit is lost is no basis for denying recovery of the costs involved. Both panels cited with approval Appalachian Electric Power Co. v. FPC, 218 F.2d 773 (4th Cir. 1955), in which a utility sought to include in regulated operating expenses litigation costs incurred in an unsuccessful lawsuit aimed at avoiding a license to construct a power plant. The Court held:

> there can be no question but that the proper expenses of the litigation should be treated, not as a general loss chargeable against earned surplus, but as an expense . . . necessary to the development of the project.[19]

The fact that a carrier is sued, or even that an adverse judgment is rendered, is no basis for assuming that the conduct giving rise to the lawsuit was imprudent. As the Second Circuit noted in Ditmars v. Commissioner, 302 F.2d 481 (2d Cir. 1962):

> What *is* ordinary is that the conduct of almost any trade or business will give rise to claims, many invalid but some valid; resisting such claims, paying judgments rendered on some, and settling others, is thus an "ordinary and necessary" expense of "carrying on any trade or business...."[20]

The sole case cited as authority for the Commission's "ratepayer benefit" standard is NAACP v. FCC, 425 U.S. 662 (1976). The panel in the Litigation Cost Decision accepted

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[19] *Id.*, 218 F.2d at 777. See Litton Accounting Appeal, 939 F.2d at 1032; Litigation Costs Decision, 939 F.2d at 1043.

[20] *Id.*, 302 F.2d at 485.

uncritically the Commission's characterization of that case.[21] The panel that decided the Litton Accounting Appeal, however, held that the Commission "has read NAACP too loosely."[22] The Court noted that in NAACP, a back pay award resulting from a finding of employment discrimination means that the company

> pays twice for work that was performed only once. The amount of the backpay award, therefore, can and should be disallowed as an unnecessary cost in a ratemaking proceeding.[23]

The Court then rejected the Commission's hypothesis that the mere fact that a violation of law has been adjudicated warrants the disallowance of the resulting costs in ratemaking.

> By our analysis, NAACP v. FPC does not underpin the Commission's unqualified and wide ranging thesis. Illegality of carrier conduct from which an antitrust litigation expense stems does not inexorably compel or warrant either rejection or stigmatization of the expense as a factor in rate calculations. As the Court made explicit, the agency "is authorized to consider the consequences of discriminatory employment practices on the part of its regulatees only insofar as such consequences are directly related to the Commission's establishment of just and reasonable rates in the public interest," and we think the Federal Communications Commission is correspondingly limited when it deals with antitrust litigation expenses. Moreover, a pervasive element in ratemaking is reasonableness,

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[21] Litigation Cost Decision, 939 F.2d at 1043.

[22] Litton Accounting Appeal, 939 F.2d at 1030.

[23] Litton Accounting Appeal, 939 F.2d at 1031.

> which demands inquiry beyond the bare fact of antitrust violation.[24]

The Commission's alternate regulatory policy grounds for the adoption of the new standard was also rejected by the Court as inadequately explained.

> The Commission has not told us what it is about violations of the federal antitrust statutes that relegates associated litigation expenses to especially unfavorable treatment. We might say the same about breaches of state antitrust statutes, and of common-law strictures, federal and nonfederal. Every lawsuit involves some claimed infraction of the law, and just why the Commission drew the line where it did remains a mystery.[25]

Thus, the Court in the Litton Accounting Appeal found that the Commission had committed two errors, one substantive and one procedural. As a substantive matter, the Commission applied an incorrect legal standard to the evaluation of litigation costs in ratemaking. As a procedural matter, the Commission failed to adequately explain or justify the policy change from the traditional ratemaking standard involving management "inefficiency or improvidence" to the "ratepayer benefit" standard. In the Notice, the Commission proposes to address the latter, procedural error, while ignoring the former, substantive error. As a result, the standard articulated in the Notice sets the stage for the Commission to commit further reversible error in this proceeding.

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[24] Litton Accounting Appeal, 939 F.2d at 1031.

[25] Litton Accounting Appeal, 939 F.2d at 1034.

The Commission's "ratepayer benefit" standard can be harmonized with the jurisprudence if the Commission equates "ratepayer benefit" with expenditures that are "necessary" to the conduct of the regulated enterprise and not "imprudently" incurred.[26] There is no need to identify a direct benefit to ratepayers in order for an expense to be necessary and prudent. It is sufficient if the expenditure is of a type ordinarily and necessarily incurred in the operation of a regulated enterprise. The defense and settlement of lawsuits, and payment after an adverse judgment, are clearly "ordinary" and "necessary" in the operation of any business. The Commission should acknowledge the appropriate legal standard and, applying that standard, reject the tentative conclusion reached in the Notice that extraordinary ratemaking treatment is required for antitrust cases or other cases alleging statutory violations.

III. The proposed litigation cost rules are unnecessary.

The proposed litigation cost rules involve changes in the Commission's accounting rules and the establishment of ratemaking presumptions. Both proposed changes are contrary to established Commission policy, and neither is adequately justified in the Notice. As shown below, both proposed changes are unnecessary and contrary to the public interest.

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[26] See NAACP v. FPC, supra.

A. Deferral accounting for litigation costs is contrary to Generally Accepted Accounting Principles.

The proposed rules require deferral accounting for litigation expenses. This proposal is contrary to Generally Accepted Accounting Principles (GAAP). There is no GAAP authority for deferring recognition of litigation costs pending the outcome of litigation. To the contrary, FASB Statement 5 requires recognition of liability resulting from litigation as soon as the outcome reasonably can be estimated. The expenses incurred in the pursuit of litigation must be recognized in the period incurred.

The cost of defending lawsuits and the payment of judgments and settlements are ordinary occurrences in the conduct of the carrier's business. GAAP requires that costs incurred in the ordinary conduct of business be charged against income in the period such charges are incurred. Therefore, the Commission's proposal to defer litigation expense to some indeterminate future period is a significant departure from GAAP.

Section 32.1 of the Commission's Rules provides:

> The Revised Uniform System of Accounts (USOA) is a historical financial accounting system which reports the results of operational and financial events in a manner which enables both management and regulators to assess these results within a specified accounting period. The USOA also provides the financial community and others with financial performance results. In order for an accounting system to fulfill these purposes, it must exhibit consistency and stability in financial reporting (including the results reported for regulatory purposes). Accordingly, the USOA has been designed to reflect stable,

> recurring financial data based to the extent regulatory considerations permit upon the consistency of the well established body of accounting theories and principles commonly referred to as generally accepted accounting principles.

The proposed accounting rules are directly contrary to these principles. The proposed accounting rules are contrary to the matching, consistency and stability principles mandated by Section 32.1, since the proposed rules will understate expenses incurred in periods in which deferral occurs and overstate expenses in the period(s) of ultimate recognition. In the Notice, the Commission neither acknowledges nor justifies this departure from the fundamental principles underlying its accounting rules.

The Notice proposes changes in accounting rules for the sole purpose of deferring litigation expenses to some future period when a decision on recoverability will be made. A presumption regarding recoverability is adopted that depends on the outcome of the litigation. If the carrier wins the lawsuit, the deferred cost would be reclassified to operating expense accounts. If the carrier loses, the deferred costs generally would be classified to a nonoperating expense account, Account 7370. Thus, the regulatory promise of recovery is contingent, not certain. Furthermore, in the increasingly competitive telecommunications environment, much of which is a result of policy initiatives by the Commission, the FCC's ability to insure recovery of costs deferred for an indeterminate period into the future is questionable. Therefore, carriers will probably be required to charge litigation expenses against current period operations in external financial reports. This would create a disparity between SEC reporting and FCC reporting. The Commission should not adopt the changes in accounting proposed in the Notice.

B. The proposed litigation cost rules are contrary to sound ratemaking policy.

In the Notice, the Commission concludes that litigation cost rules represent necessary changes in ratemaking policy for AT&T, the price cap local exchange carriers ("LECs") and the more than 1300 smaller LECs. As shown below, the Commission's rationale as to each group of carriers is faulty and should be rejected.

The only rationale offered in the Notice for adopting the proposed litigation cost rules with regard to AT&T is the purely circular statement:

> AT&T and the LECs must still maintain regulated books of accounts, and the accounts must continue to be kept in accordance with the rules and policies of this Commission.[27]

While this statement is a truism, it does not discuss, much yet justify, a change in Commission policy. AT&T operates under a pure price cap plan. Therefore, the unique accounting treatment proposed in the Notice will have no impact whatsoever on AT&T's rates to its customers. Hence, it will produce no ratepayer benefit. It will, however,

[27] Notice at para. 7.

cause AT&T to incur unnecessary costs to track these expenses and maintain separate regulatory accounting, thereby diminishing AT&T's efficiency and placing it at a competitive disadvantage vis-a-vis other interexchange carriers not subject to the unique accounting rule. There is no justification in the Notice, and BellSouth perceives none, for adopting such a requirement for AT&T.

With regard to the price cap LECs, the same rationale applies. The only difference in the situation of price cap LECs and AT&T is the existence of the sharing mechanism in the LEC price cap plan. The existence of the sharing mechanism makes it particularly inappropriate to apply the litigation cost rules proposed in the Notice to price cap LECs. Because legitimate operating costs are not recognized in the year in which they are incurred, the proposed rules could drive a carrier's regulated return into the sharing range, or increase the amount of the sharing obligation, years prior to an adjudication of the merits of the underlying lawsuit. Conversely, in the year in which a lawsuit is resolved favorably to a price cap LEC, many years of deferred litigation costs may be recognized, thereby reducing or eliminating a sharing obligation in that period. Thus, the application of the proposed rules to price cap LECs would have a disparate impact on the effected carriers based solely on the carrier's earnings in the year an alleged antitrust violation is adjudicated.

An antitrust violation can be adjudicated against a price cap LEC only many years after the alleged violation occurred. The possibility that the accused LEC will be in the sharing range in the year of adjudication would be purely happenstance. Therefore, whether the proposed disallowance is actually reflected in carrier rates would be wholly unrelated to the conduct giving rise to the Commission's concerns. The accounting treatment of litigation costs proposed for price cap LECs would result in disparate treatment of similarly situated carriers based solely on the earnings of the carrier years after the event triggering the application of the rule. Such a result would be arbitrary and capricious.

An additional reason to reject application of the proposed rules to price cap LECs is that such an application would, in aggregate, double count the proposed adjustment. The Commission's prior litigation cost accounting rules were applied by carriers from their adoption in 1987 until the Court of Appeals vacated the Commission's rules in 1991. In the meantime, the initial rates for price cap LECs were established, effective January 1, 1991, based on rates in effect as of July 1, 1990. Thus, the impact effect of the now vacated rules was built into the initial price cap rates. For the Commission to now seek to apply new adjustments to the price cap LECs would double count the effect of the litigation cost rules.

Nor should the Commission adopt the proposed policy for non-price cap LECs. Although numerous, the non-price cap LECs are basically small carriers who are much less likely to be the target of an antitrust lawsuit. Furthermore, the burden of tracking and the cost of deferred recognition of legitimately incurred operating costs will impact more severely on these smaller carriers. Furthermore, it may be expected that even if a non-price cap LEC were found guilty of an antitrust violation, the resulting damages, and hence disallowances, would be relatively small. Thus, the perceived ratepayer benefit from application of the proposed rule to non-price cap LECs would likely be inconsequential to customers.

As noted above, the Commission's rules require that carriers subject to Part 32 generally follow GAAP accounting. GAAP accounting places the regulatory books of a carrier on an equal footing with the books of its competitors not subject to Part 32. The Notice, however, does not propose to impose the litigation cost rules on nondominant interexchange carriers, competitive access providers, cable companies, and other competitors of Part 32 carriers. Thus, the proposed rules single out carriers subject to Part 32 for unique and unfavorable accounting and ratemaking treatment not imposed upon other carriers subject to the Commission's jurisdiction. The Commission neither acknowledges nor justifies this discriminatory treatment of

Part 32 carriers. The Commission's tentative conclusion that the proposed litigation cost rules are necessary is erroneous, and should be rejected.

IV. The proposed litigation cost rules will impose costs, both direct and indirect, on the carriers and their customers that far exceed any perceived benefit.

As shown above, the proposed litigation cost rules will provide little benefit to ratepayers. They will, however, impose both direct and indirect costs to carriers and their customers that far exceed any perceived benefit.

A. The direct costs that will be borne by ratepayers if the Commission adopts the proposed rules are significant.

First, there are the direct costs involved by the carriers in tracking and reporting lawsuits encompassed by the rule. Based on experience gained prior to the Court's action vacating the prior rules, BellSouth can identify substantial costs that will be incurred by the carriers and borne by ratepayers if the proposed rules are adopted.

Each lawsuit that is filed against a carrier subject to litigation cost rules must be reviewed by an attorney to determine whether the triggering criteria of the rule are met. If so, the costs incurred in defending the suit must be segregated from ordinary operating costs on an ongoing basis and reported to the appropriate account. As the litigation progresses, the lawsuit must be monitored to determine if the triggering counts of the complaint are resolved at a preliminary stage of the proceeding in favor of the defendant. If so, the costs deferred must be